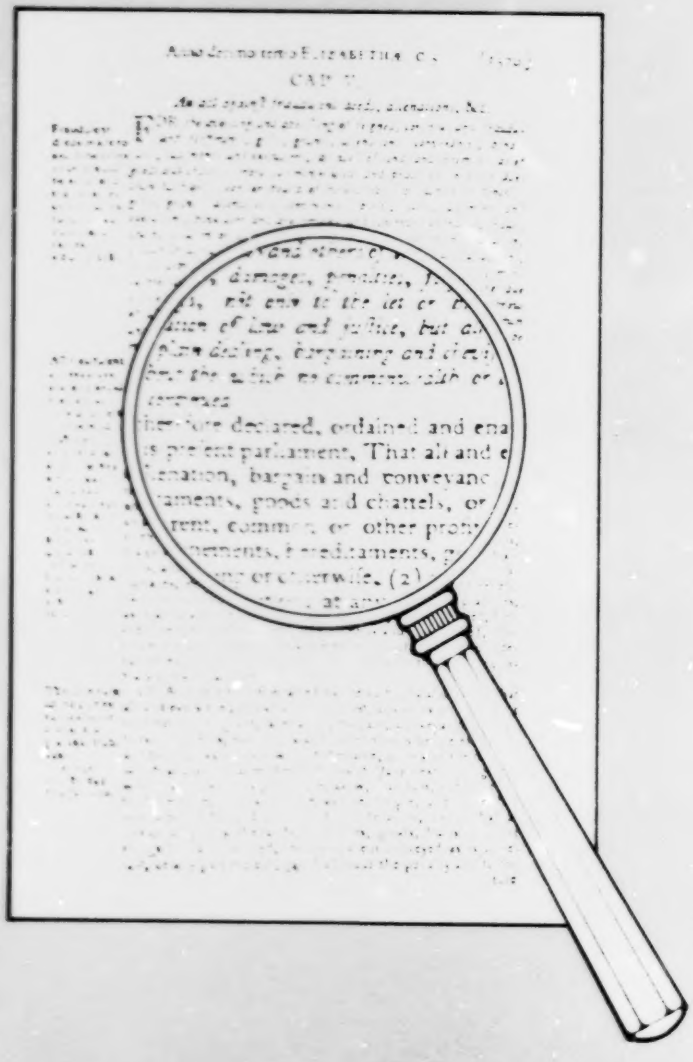
Law Reform Commission of Saskatchewan

Proposals Relating to Ademption by Equitable Conversion

Report to the Minister of Justice

Saskatchewan



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PROPOSALS RELATING TO ADEMPTION BY EQUITABLE CONVERSION

Law Reform Commission of Saskatchewan
Saskatoon, Saskatchewan

Report to the Minister of Justice

October, 1984

The Law Reform Commission of Saskatchewan was established by *An Act to Establish a Law Reform Commission* proclaimed in November, 1973, and began functioning in February of 1974.

The Commissioners are:

Professor DOUGLAS A. SCHMEISER, Q.C., B.A., LL.B., LL.M., S.J.D., Chairman

Miss MARJORIE A. GERWING, Q.C., B.A., LL.B.

Mr. GORDON J. KUSKI, Q.C., LL.B.

Mr. Kenneth P. R. Hodges, B.A., LL.B. is Director of Research.

Mr. Michael J. W. Finley, B.A., M.A., LL.B. and Mr. C. Peter Thagard, LL.B. are the Legal Research Officers, and Mr. Roderick J. Wood, LL.B., LL.M., Dip. in Legislative Drafting and Mrs. Sandy Antonini-Ready, LL.B. are Legal Research Officers under contract. The secretaries are Mrs. Sandra Ritchie and Miss Pat Harasymchuk.

Mrs. Pam Haidenger-Bains, Barrister and Solicitor, Saskatoon, Saskatchewan served as Consultant to the Commission on ademption by equitable conversion.

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The Law Reform Commission Act.

6. The commission shall take and keep under review all the law of the province, including statute law, common law and judicial decisions, with a view to its systematic development and reform, including the codification, elimination of anomalies, repeal of obsolete and unnecessary enactments, reduction in the number of separate enactments and generally the simplification and modernization of the law.

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Saskatchewan

Law Reform
Commission of
Saskatchewan

Provincial Office Building
122 Third Avenue North
Saskatoon, Canada
S7K 2H6

(306) 664-6127

The Honourable J. Gary Lane, Q.C.
Minister of Justice
Province of Saskatchewan
Regina, Saskatchewan

Dear Mr. Minister:

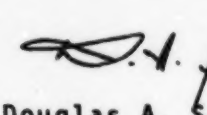
The Commission has completed its examination of ademption by equitable conversion.

Ademption by equitable conversion is a relatively obscure legal rule, but despite its obscurity - or perhaps because of it - the rule can have unfortunate and unanticipated consequences. The rule provides that a testamentary gift fails if there is a change in the nature of the property devised. It was applied recently by the Saskatchewan Court of Appeal in Re McMurdo, where a gift of land by will to a friend of the testator was defeated merely because the testator had entered into an agreement for sale with the friend prior to death. The Commission wishes to thank Mr. Justice Tallis of the Court of Appeal for bringing this problem to its attention.

Some Canadian provinces, including Alberta, Ontario, New Brunswick and Newfoundland, have addressed the problem through legislation. This report also proposes a legislative solution, although in somewhat different terms than in those jurisdictions.

Pursuant to section 9 of The Law Reform Commission Act, the Commission submits this report recommending amendment of The Wills Act.

Respectfully submitted this 1st day of October, A.D. 1984.



Douglas A. Schmeiser, Q.C.,
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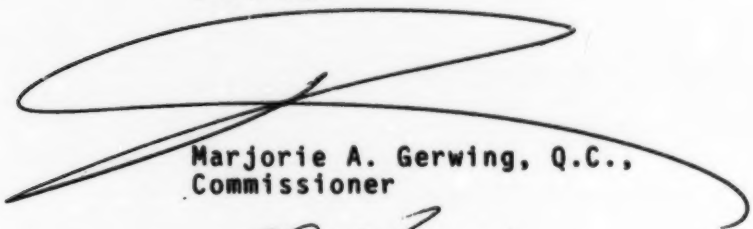
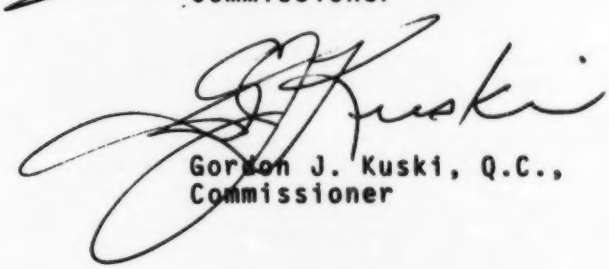


Marjorie A. Gerwing, Q.C.,
Commissioner



Gordon J. Kuski, Q.C.,
Commissioner

PROPOSALS RELATING TO ADEMPTION BY EQUITABLE CONVERSION

I. INTRODUCTION

In December of 1970, William Thomas McMurdo of Maple Creek, Saskatchewan, made his last will and testament. He left 320 acres of farmland to his "young friend, Jack Cameron". In 1975, McMurdo entered into an agreement with Cameron for sale of the land. Under the terms of the agreement, Cameron took possession of the land and agreed to pay the purchase price in eleven annual instalments. When McMurdo died in 1979, a substantial part of the purchase price had not yet been paid.

Court proceedings were commenced to determine whether Cameron was entitled to take the land without any obligation to pay the balance of the purchase price. There appears to have been evidence that this was the result intended by McMurdo. However, the trial judge ruled that Cameron was obligated to pay the balance of the purchase price.[1] The Saskatchewan Court of Appeal dismissed Cameron's appeal,[2] considering itself bound by a previous decision of the Supreme Court of Canada[3] to hold that the gift in the will failed because of the subsequent sale.

In the result, Cameron received nothing under McMurdo's will. Had he not entered into the agreement for sale, he would have been entitled under the will to the land without payment.

Cameron was unsuccessful at trial and on appeal because of the rule that a specific gift in a will fails if the subject matter of the gift has ceased to exist as part of the testator's property in his lifetime. This is known as the ademption rule.[4] Where a testamentary gift is adeemed, the beneficiary named in the will cannot look to other assets of the estate to replace the gift, nor in this case was Cameron entitled to the testator's interest in the agreement for sale.

Ademption can occur in various ways, including destruction, loss, theft, expropriation, foreclosure, seizure, gift or sale. The *McMurdo* case involved ademption by equitable conversion. Ademption by equitable conversion may occur when a testator enters into an agreement for sale of property previously devised by his will. The reason is that the transaction changes the nature of the testator's interest in the property.[5]

As the *McMurdo* decision illustrates, this aspect of the ademption rule can yield harsh results. In the course of rendering the judgment of the Court of Appeal, Mr. Justice Tallis expressed regret concerning the decision that the Court found itself bound to make:

> In some jurisdictions legislation has been enacted to correct what the learned justices [of the Supreme Court of Canada] considered to be an injustice. Perhaps the legislature of this province may, in its wisdom decide to consider such changes.[6]

This report proposes changes in the law regarding ademption by equitable conversion. In addition, it considers the advisability of further changes to the ademption rule.

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1 *Re McMurdo*, Sask. Q.B., July 17, 1980 (unreported).

2 *Re McMurdo* (1982), 131 D.L.R. (3d) 454; *sub nom. McMurdo Estate*; *Gold v. Cameron* (1982), 14 Sask. R. 220.

3 *Church v. Hill*, [1923] S.C.R. 642; *sub nom. In re Church*, [1923] 3 W.W.R. 405.

4 See *Hals. Laws*, 3d Ed., Vol. 39, at 934-35; also, Thomas G. Feeney, *The Canadian Law of Wills: Construction*, Toronto: Butterworths, 1978, at 172-73.

5 Equitable conversion is discussed in *Hals. Laws*, 3d. Ed., Vol. 14, 576.

6 (1982), 131 D.L.R. (3d) 454, at 461; (1982), 14 Sask. R. 220, at 229.

II. ADEMPTION AND EQUITABLE CONVERSION

Two reasons can be stated for the existence of the ademption rule. The first is based on the presumed intention of the testator. If a testator has left his will unchanged after property has been sold, destroyed or lost, the inference can be drawn that he intended to revoke a specific devise or bequest of the property. Ademption, however, does not depend on proof of actual intention, and in fact operates independently of intention.

The second and more compelling reason for the existence of the rule is the difficulty of substituting other estate assets for the specific property named in the will. If a particular chattel described in a will is no longer owned by the testator at his death, how can it be inferred that the testator would have wanted the legatee named in the will to have received some other chattel or a cash sum in lieu thereof? If the will itself contains words indicating some such intention, ademption will be avoided, but not otherwise.

It is more difficult to rationalize ademption that results from the doctrine of equitable conversion, sometimes referred to as "notional" conversion. A change in the nature of property that is the subject matter of a specific gift will result in an ademption of the gift. For example, it is well settled that an agreement for sale of land converts the vendor's interest from realty to personalty.[7] This conversion has been held to occur even though the legal title to land ordinarily remains in the vendor until an agreement for sale is paid out.[8] Thus, where land is devised to a beneficiary and the land is subsequently made subject to an agreement for sale, the devise is adeemed by equitable conversion. This is so whether the sale is to a third party[9] or to the beneficiary named in the will.[10] Similarly, where devised land is sold by a testator who takes back a mortgage to secure part of the purchase price, the devise is adeemed.[11] Although the granting of an option to purchase does not per se create an equitable conversion, such will be the result when the option is exercised, even if it is exercised after the testator's death.[12]

In each of the above cases the beneficiary named in the will cannot claim the proceeds from the agreement for sale, mortgage, or option agreement. A reading of *The Wills Act*, R.S.S. 1978, c.W-14, would have suggested a contrary result. Section 20 reads as follows:

> No conveyance or other act relating to any real or personal property comprised in a will, made or done subsequent to the execution of the will, shall prevent the operation of the will with respect to such estate or interest as the testator had power to dispose of by will at the time of his death.

This section can be traced back to the Saskatchewan Statutes of 1907, and has its origin in the English *Wills Act, 1837*, 1 Vict. c.26. The section was not designed to oust the doctrine of equitable conversion. It was designed to ensure that, for example, where a testator devised land in which he had a leasehold interest at the time of making his will and subsequently acquired the fee simple estate, the devise would pass the fee simple.[13] It would also apply where a testator devised land and

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[7] *Church v. Hill*, *supra* note 3; see also Thomas G. Feeney, *The Canadian Law of Wills: Construction*, *supra* note 4, at 201-02; the rationale is that, because equity considers as done that which ought to be done, the vendor's interest is converted into money.

[8] *Church v. Hill*, *supra* note 3.

[9] *Ibid*.

[10] *Wormsbecker v. Wormsbecker and Wormsbecker*, [1947] 2 W.W.R. 940 (Sask. C.A.).

[11] *Hicks v. McClure* (1922), 64 S.C.R. 361; 70 D.L.R. 287.

[12] *Re Rodger*, [1967] 1 O.R. 379; (1966), 60 D.L.R. (2d) 666 (Ont. H. Ct.).

[13] Stephen Cretney and Gerald Dworkin, *Theobald on Wills*, 13th ed., London: Stevens and Sons, 1971, at 200.

subsequently mortgaged or leased it.[14] In this context, it is significant that at one time a mortgage amounted to a conveyance of the legal title to land, so that without the *Wills Act* provision the very act of mortgaging the land would have resulted in ademption of a devise of the land. However, a series of nineteenth century English cases established that the provision did not apply to prevent ademption by equitable conversion of land.[15] This interpretation has been accepted in Canada in numerous decisions, and was adopted by the Supreme Court of Canada in *Church v. Hill*.[16] The issue having been settled, section 20 of *The Wills Act*, R.S.S. 1978, c. W-14, was not referred to in the reasons for judgment in *Re McMurdo*. Left to apply the doctrine of equitable conversion, the Saskatchewan Court of Appeal had no choice but to hold that the devise had adeemed

III. ANALYSIS OF THE PROBLEM

As the *McMurdo* case illustrates, there are situations where ademption operates to frustrate a testator's intention. There also will be situations where ademption by equitable conversion serves to carry out a testator's intention to revoke a gift contained in his will. For example, a testator may find that his financial position has deteriorated after making his will. He might sell the devised property by agreement for sale, intending the payments to support his family during his lifetime and afterwards. In that situation, the testator might intend the gift in the will to fail. Thus, it is no easy task to construct a rule that will produce a fair result in every case.

The root of the problem is a rule fundamental to the construction of wills: a testator's intention must be deduced from the words of the will itself.[17] In the context of ademption, the words of the will usually provide no clue as to the testator's intentions. This is because a testator who includes in his will a specific gift will ordinarily not be contemplating sale or loss of the property. The usual case will be that a person making a specific devise or bequest has every intention of retaining the property until his death. Unfortunately, circumstances may change. Unforeseen events may occur. Property may be destroyed by fire. A chattel may be lost or stolen. Hard economic times may force a sale of assets that a testator had previously intended to keep until the end of his life. Even if a testator actually contemplated what ought to happen to the gift contained in his will in the event of such circumstances, it is doubtful that the result of his deliberations will be ascertainable from the words of his will. We are left to speculate what the testator must have intended.

The rule of ademption resolves the issue by concluding that a testator intended to revoke a gift where the subject matter of the gift has ceased to be part of his estate. There is some logic in this result; in cases where property that is the subject of a testamentary gift is sold, lost or destroyed, it is always open to the testator to change his will. If he does not do so, it can be assumed that his intention is to revoke the gift. Unfortunately, this assumption fails to take into consideration the possibility that the testator has not directed his mind to the legal effect of the sale or loss of the chattel. Alternatively, the testator may have misunderstood the legal consequences of the sale or loss. Or, human nature being what it is, the testator may have realized the effect and resolved to change his will, but failed to take the necessary steps to do so.

Although it seems that at one time evidence of the testator's actual intention could be looked to in deciding whether or not ademption should come into play,[18] consideration of actual intention was long ago replaced by the modern ademption rule. Still, the difficulty inherent in attributing a

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[14] See the *dicta* of Shadwell, V.-C., in *Moor v. Raisbeck* (1841), 59 E.R. 1078, All E.R. Reprints (1835-1842) 516, at 520.

[15] For example, *Moor v. Raisbeck*, *supra* note 14.

[16] [1923] S.C.R. 642, at 644; 3 W.W.R. 405, at 407.

[17] Feeney, *The Canadian Law of Wills: Construction*, *supra*, note 4, at 13.

[18] The suggestion is made in Thomas Jarmen, *A Treatise on Wills*, 8th Ed., Toronto: Carswell, 1951 at 1066.

like intention to all testators in all fact situations is readily apparent. One possible solution would be to replace the rule with a presumption rebuttable by extrinsic evidence of the testator's actual intention. In the *McMurdo* case, where it appears there was evidence available as to the real intention of the testator, a presumption of ademption would likely have been rebutted, thus producing a result that, in the opinion of the Court of Appeal, would have been fairer. The Commission, however, is unable to recommend such a change. To tackle the ademption problem by looking to extrinsic evidence of the testator's actual intention would lead to uncertainty about the effect of a will and would result in litigation whenever the problem arose.

We are left with a choice of inflexible rules. Either a gift is always adeemed in given circumstances or it is never adeemed. Obviously, the ademption rule cannot be dispensed with in all situations. Where a substitution or tracing problem exists, the only practical answer is that the gift must fail. On the other hand, where the proceeds from the property are easily identifiable, there will be situations in which it is appropriate to assume that the testator would have wished to favour the specific legatee over the residuary legatee. The Commission is of the opinion that the *McMurdo* situation, where there was a subsequent agreement for sale between the testator and the beneficiary, is one such situation. The obligation of the beneficiary to make payments under the agreement for sale should terminate upon the death of the testator.

Should the ademption rule also be reversed where the agreement for sale is with a third party? The Supreme Court of Canada in the *Church* case thought so, and the Saskatchewan Court of Appeal in *McMurdo* apparently thought likewise. The Commission agrees. When a person makes a will disposing of real property and later agrees to sell it but still retains the legal title, he generally considers that he still owns the property and that it remains subject to his testamentary disposition until he has completed the actual conveyance of legal title. This concept of "title" is paramount in the minds of many Saskatchewan property owners. A vendor of land who retains the duplicate certificate of title (which he considers to be his "title") might well be surprised to learn that a devise in his will of all his interest in the property has been rendered ineffective by the agreement for sale.

Some of the same considerations apply where a testator sells land and secures the purchase price by taking back a mortgage. In such a case the purchaser immediately becomes the registered owner and the vendor does not retain "title". On balance the Commission feels that a testator in such circumstances would be more likely to intend that the beneficiary take the benefit of the mortgage, particularly so where the beneficiary is the purchaser/mortgagor. The testator might reasonably expect that a gift of "all my interest in Blackacre" would include his interest as mortgagee. An additional consideration is that an agreement for sale and a mortgage back are two common ways of effecting financing. For the most part, these two methods of arranging financing produce equivalent legal consequences. It would be undesirable to treat them differently in the context of ademption.

Another area for consideration relates to options to purchase. The Commission is of the opinion that a devisee of land that is subsequently made subject to an option to purchase ought to inherit the land, subject to the option. The arguments against ademption by equitable conversion in the case of an option to purchase are even stronger than in the case of an agreement for sale, in that an option represents only a possibility of a future sale. A testator who grants an option likely would be surprised to learn that a devise of the land is adeemed if the option is exercised after his death.

Other jurisdictions have gone further in reducing the scope of ademption. The Ontario legislation entitles a beneficiary to claim insurance proceeds where the subject matter of the gift has been lost or damaged.[19] If property is expropriated, the beneficiary named in the will takes the compensation payable in respect of the property.[20] The Commission does not recommend altering

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[19] *The Succession Law Reform Act*, R.S.O. 1980, c. 488, subsection 20(2).

[20] *Ibid*.

the ademption rule in cases, such as the above, where conversion of the property is involuntary. Destruction or expropriation of the property should signal to the testator the need for a change of will if he wishes the beneficiary to take under his will. This can be distinguished from a situation where a testator retains an interest in the property and likely expects that the words in his will are sufficient to pass such interest.

Similarly, the Commission does not recommend altering the ademption rule where a testator voluntarily divests himself of his entire interest in property. The provision recommended by the Uniform Law Conference, which has been substantially adopted by Alberta and New Brunswick, in addition to Ontario, entitles a beneficiary to claim any "right or chose in action or equitable estate or interest" created by a contract involving a conveyance of the property.[21] This would include a promissory note or even the purchaser's cheque, and goes too far. As well, the "right or chose in action or equitable estate or interest" need not be referable to the devised or bequeathed property. For example, if a testator, having devised Blackacre, sells Blackacre and as part of the consideration for the sale receives a leasehold interest in Whiteacre, the beneficiary named in the will takes the interest in Whiteacre. This goes further than necessary to remedy the problem caused by the interpretation given to section 20 of our Act.

Finally, it is recommended that the rule of ademption not be altered insofar as personal property is concerned. For one thing, only rarely will a testator who sells personal property retain an interest in the property. More significantly, the commonly held concept of legal title to real property does not apply to personal property.

IV. RECOMMENDATIONS

How can the changes suggested above best be implemented? Earlier in this report, the restrictive interpretation that has been placed on section 20 of *The Wills Act* was noted. The logical solution is to alter section 20. It has been recommended in this report that the ademption rule be altered only where a testator after making his will sells the property under an agreement for sale, transfers the property and takes a mortgage back, or grants an option to purchase the property. This result can be achieved by adding a new subsection to section 20, so that the section would read as follows:

> (1) No conveyance or other act relating to any real or personal property comprised in a will, made or done subsequent to the execution of the will, shall prevent the operation of the will with respect to such estate or interest as the testator had power to dispose of by will at the time of his death.
>
> (2) Unless a contrary intention appears in the will, where a testator has devised real property and subsequently:
>
> (a) sells the property by agreement for sale;
>
> (b) sells the property and takes back a mortgage thereon as security for all or part of the purchase price; or

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[21] Section 21 of *The Uniform Wills Act* reads as follows:

(1) A conveyance of or other act relating to real or personal property comprised in a devise or bequest or other disposition made or done after the making of a will, does not prevent operation of the will with respect to any estate or interest in the property that the testator had power to dispose of by will at the time of his death.

(2) Except when a contrary intention appears by the will, where a testator at the time of his death has a right or chose in action or equitable estate or interest that was created by a contract respecting a conveyance of, or other act relating to real or personal property that was comprised in a devise or bequest, made or done after the making of a will, the devisee or donee of that real or personal property takes the right or chose in action or equitable estate or interest of the testator.

(c) grants an option to purchase the property;

the beneficiary named in the devise takes the testator's interest under the agreement for sale, mortgage or option agreement.

Where other provinces have amended the equivalent section in their wills legislation, a consequential amendment has in each case been made to the provision equivalent to section 21 of our *Wills Act*. The Saskatchewan provision reads as follows:

> 21. Unless a contrary intention appears by the will every will shall be construed, with reference to the real and personal property comprised in it, to speak and take effect as if it had been executed immediately before the death of the testator.

Other provinces have extended the section to "a right to chose in action or equitable estate or interest to [proceeds]" or have used words of like effect.[22] It may be argued that the consequential amendment was unnecessary; a chose in action, for example, is necessarily personalty,[23] and is therefore covered by "real and personal property". Because of the different approach taken herein, an analogous consequential amendment is unnecessary.

V. SUMMARY OF RECOMMENDATIONS

The Commission recommends that where a testator devises real property and subsequently sells the property under an agreement for sale, transfers the property and takes back a mortgage, or grants an option to purchase the property, the devise does not adeem, and the beneficiary takes the interest of the testator under the agreement for sale, mortgage or option agreement.

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[22] See, for example, the *Uniform Wills Act*, subsection 21(2), or Alberta's *Wills Act*, R.S.A. 1980, c. W-11, section 22.

[23] This conclusion follows from a reading of *Halsbury's Laws of England*, 3rd Ed., Vol. 29, 355-359, under the topic "Personal Property". A contrary inference, however, could be drawn from the Supreme Court of Canada decision in *Thorne v. Thorne* (1903), 33 S.C.R. 309, where it was held that a devise by will of "all my . . . property whatsoever" did not include a debt due to the testator from the beneficiary's firm. Thus, the *Thorne* decision may have been the impetus for the consequential amendment. On the other hand, nothing in the reasons for judgment suggests that any attempt was made to analyze the nature of a chose in action. At issue was the intention of the testator, and the court concluded that because "in ordinary parlance a chose in action is not called property", the testator did not mean to include the debt. It is suggested that there is ample authority for the proposition that a vendor's interest under an agreement for sale is personal property; see, for instance, Victor Di Castri, *Law of Vendor and Purchaser in Canada*, 2nd Ed., Toronto: Carswell, 1976, at 13.